No. 84-175

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1984

GEORGE BROOKS SCHREIBER, *Petitioner*,

v.

GENCORP., INC., et al., *Respondents*.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF OF SHAREHOLDER RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the Court of Appeals should have set aside as a clear abuse of discretion the approval of a settlement terminating the case at bar.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES: *PAGE*

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STATEMENT OF CASE

The petitioner, George Brooks Schreiber, requests that this court grant a Writ of *Certiorari* in order to prevent a termination of litigation begun in 1976 and to which all parties to the matter had agreed to settle in 1981. In seeking review the petitioner raises no constitutional question nor does he seek review of any question of federal law. Rather, the petitioner would have this Court review the fairness of a settlement which was approved both by the United States District Court for the

Northern District of Ohio and the United States Court of Appeals for the Sixth Circuit. For the reasons set forth below the shareholder respondents[1] respectfully submit that there is no basis whatsoever for disturbing the decision of the Court of Appeals and that the case *sub judice* should be allowed a long overdue repose.

This litigation arises from the participation of respondent GenCorp., Inc., formerly known as The General Tire & Rubber Company (hereinafter GenCorp.) in a program during the 1960's and 1970's to obtain favors from foreign and domestic political officials in return for payments variously characterized as bribes, campaign contributions and expediting payments. These payments were made secretly without the knowledge or the consent of the shareholders of GenCorp. and only came to light on May 10, 1976 when the corporation and the Securities and Exchange Commission (hereinafter SEC) entered into a consent decree of that date. Under the terms of the consent decree the corporation and its chief executive officer agreed to be restrained from participating from making any future unlawful payments to foreign officials or unlawful domestic political contributions and from engaging in practices designed to prevent disclosure of such improper payments. It was also agreed that a special committee of the Board of Directors of the corporation would conduct an investigation into the past practices of the corporation and make recommendations to prevent its reoccurrence.

Following the entry of the SEC consent decree four shareholder derivative suits were filed on behalf of the corporation against certain of GenCorp.'s officers and directors seeking remedial relief to prevent future improper payments from being

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[1]This brief is submitted on behalf of Harry Lewis, Mitchell A. Kramer, Betty Ann Weintraub, Alter Milberg, Arthur L. Monheit and Dorothy Monheit, Administrator of the Estate of Charles Monheit all of whom are plaintiffs in the shareholder derivative actions described below.

made as well as damages.[2] These four complaints, filed in the districts of New Jersey, Pennsylvania and Ohio in 1976 were consolidated before the United States District Court for the Northern District of Ohio pursuant to 28 U.S.C. §1407 in the following year. *In re General Tire & Rubber Company Securities Litigation*, 429 F. Supp. 1032 (J.P.M.D.L. 1977). In 1980 four additional derivative actions were commenced on behalf of the corporation in both the State and Federal Courts of New York and in the State Courts of Delaware.[3] These actions were filed in response to an announcement in January of 1980 that the Federal Communications Commission (hereinafter FCC) had determined to deny renewal of three broadcasting licenses held by RKO General, a subsidiary of GenCorp. The derivative actions alleged that the action of the FCC was a result of the improper payment practices noted above and sought damages for the loss of the broadcast licenses. The settlement which the petitioner seeks to abort would terminate all eight proceedings.

During the course of the shareholder litigation begun in 1976 two significant events moved the parties towards the settlement ultimately reached in 1981. The first was the judicial evolution of the business judgment defense. The business judg-

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[2]The four initial actions were *Betty Ann Weintraub as Successor In Interest to David Cohn* v. *John O'Neil, et al.*, District of New Jersey, Civ. Action No. 76-1006; *Mitchell A. Cramer* v. *The General Tire & Rubber Company, et al.*, Eastern District of Pennsylvania, Civil Action No. 76-1525; *Alter Milberg* v. *The General Tire & Rubber Company, et al.*, Southern District of Ohio, Civil Action No. C-1-76-323; and *Harry Lewis* v. *Michael G. O'Neil, et al.*, Northern District of Ohio, Civil Action No. C-76-344A.

[3]The four additional derivative actions are *Kaufman* v. *Garvin, et al.*, New York Sup. Court, Index No. 67231/80; *Bar* v. *O'Neil, et al.*, N.Y. Sup. Court, Index No. 67241/80; *Monheit* v. *O'Neil, et al.*, Del. Ch. Civ. No. 6149. The *Monheit* federal action was transferred to the Northern District of Ohio for purposes of settlement while the parties to the State Court suit agreed that such litigation would be terminated upon approval of the settlement on the grounds of *res judicata*.

ment rule essentially states that the decision whether or not to bring a lawsuit for damages against corporate directors or officers is like any other business decision, a matter left to the discretion of the Board of Directors of the corporation. Thus, it has been reasoned that if directors either refuse to bring a suit on behalf of the corporation or believe that such a suit in the form of a derivative action is against the best interests of the corporation they have the power to terminate litigation unless the directors themselves stand in such a position that they are unable to provide an unprejudiced exercise of judgment. While first enunciated in 1917 the business judgment rule was rarely invoked in the course of derivative litigation brought in the 1960's or 1970's. However, subsequent to the initiation of the case *sub judice and the filing of a motion for summary judgment by the corporation and its directors under this rule in 1977, a spate of decisions were announced throughout the country, virtually all of them unfavorable to the position held by the shareholder respondents that the business judgment rule would not apply to the case sub judice.* Accordingly, at the time of the settlement in 1981 shareholders recognized that there was a very high probability that their derivative actions would be dismissed under this defense.

A second factor that led to the 1981 settlement was a series of reforms undertaken by the corporation to assure that the improper conduct complained of in the shareholders' complaints would not be repeated. During the course of the shareholder litigation the corporation altered its internal auditing procedures, enlarged the scope of review of its independent accountants, revised the procedures utilized by its subsidiary RKO in recording certain types of transactions and also required that certain officers and directors reimburse the corporation in the amount of $337,260. Order of Judge Batisti dated December 15, 1981 shareholder respondents Appendix A (hereinafter referred to as appendix SRA) p. 2. Thus, the pressure exerted by shareholders through the maintenance of derivative complaints resulted in the effectuation of the very reforms the shareholders sought in the litigation. Accordingly,

by the Spring of 1981 the shareholder respondents recognized that the likelihood of success on the merits was small and that much of what they had sought to accomplish had already been put into place. Further litigation in what was then a five year old case might well have resulted in no benefit to the corporation and great cost and expense to all litigants. This belief was reenforced by discovery taken in the Spring of 1981 by the shareholder respondents in which after review of documents and the taking of various depositions, little could be garnered that could be effectively used to establish that the directors in question lacked the independence required for them to utilize the business judgment defense. Accordingly, after several months of negotiations among all parties a Stipulation of Settlement was filed with the District Court on June 25, 1981.

The settlement in question acknowledged that the directors of the corporation had the right as a matter of law to seek termination of the litigation under the business judgment rule. It further acknowledged the role of the shareholders in causing the company to undertake the program of remedial action to prevent a reoccurrence of the improprieties in question. Further, the settlement provided that at least two directors of RKO's Board of Directors would be outside directors, *i.e.*, neither officers nor employees of RKO. The settlement also called for a dismissal of the eight shareholder actions and provided that the corporation would pay up to a certain amount of any counsel fees awarded to counsel for the shareholders for their efforts in this matter.

A Notice of Hearing and Proposed Settlement was sent to all of GenCorp.'s shareholders to inform them of the nature of the settlement and afford any shareholder the opportunity to be heard at the settlement hearing scheduled for August 18, 1981. Only five of the corporation's approximately 50,000 shareholders filed objections and only two, the petitioner and John A. Curtis Pearl entered an appearance at the settlement hearing. Before passing upon the fairness of the proposed settlement the District Court permitted both objectors to argue at the August 18th hearing and allowed them an opportunity

to examine all discovery taken in the matter and the right to present additional written submissions to the court, which both objectors in fact did. The District Court in its order of December 15, 1981 after carefully considering all of the various objections raised by the petitioner found that in fact the settlement was fair, reasonable and adequate. Specifically, the District Court after considering existing law on the Business Judgment Rule and reviewing the facts presented on the independence of the directors who sought dismissal through said rule found that the shareholders "would have faced considerable difficulties had they brought this litigation to trial"; and that "the premonition of an adverse summary judgment in the thinking of plaintiffs' counsel (shareholder respondents) cannot be faulted". Appendix SRA pp. 12-13. The court also found the small number of objections filed and the benefits to be derived from the addition of outside directors to the Board of Directors of RKO led to the conclusion that the proposed settlement adequately protected the parties involved in this lengthy and complex litigation. In addition, in approving the settlement in question the District Court denied the motion by the petitioner herein to be allowed to intervene in the matter. Most significantly the District Court found that counsel for the objector, who had until a short time prior been counsel of record before the FCC on behalf of a company vigorously seeking to have an RKO broadcast license revoked, should not be allowed to intervene as counsel for the shareholders in the case at bar. Rather, the District Court found good cause to believe that the petitioner-objector was "not able to fairly and adequately represent the interest of the corporation". Appendix SRA p. 15.

In its decision of January 13, 1984 the Court of Appeals for the Sixth Circuit affirmed the District Court's approval of the settlement in question and denial of the motion to intervene. The Court of Appeals first found that the District Court had not abused its discretion in determining the manner in which the business judgment rule would apply in this matter. Accordingly, it held that in view of the slight possibility that the shareholders would have been successful in pursuing their

derivative actions the District Court was "well within in its discretion when it determined that the settlement was 'reasonable, fair and adequate'". Petitioner's Appendix A, p. 18. In the absence of any evidence that the District Court had abused its discretion the Sixth Circuit affirmed the District Court's decision in all respects including denial of the petitioner's right to intervene.

The shareholder respondents respectfully submit that the affirmance by the Court of Appeals should be allowed to terminate this matter. As analyzed below there are simply no special or important issues raised by this appeal and there is no basis for the Court to take the extraordinary step of granting a Writ of *Certiorari* to review whether a settlement approved both by the District Court and the Court of Appeals should be overturned.

ARGUMENT

THE CASE AT BAR DOES NOT RAISE ANY SPECIAL OR IMPORTANT REASONS THAT WOULD JUSTIFY GRANTING REVIEW ON CERTIORARI

Rule 17 of the Rules of the Supreme Court states that a Writ of *Certiorari* will only be granted when there are special or important reasons therefor. In seeking *certiorari* the petitioner does not claim that there has been a decision on any important question of federal law involved in this matter. Rather, the petition is limited to an argument that the decision of the Court of Appeals in this matter conflicts with a decision of at least one other Circuit. Alternatively, it is urged that this Court utilize its supervisory power to correct improprieties alleged to have been taken by the Court of Appeals in rendering its decision. As discussed below neither claim contains any substance and the petition is merely a request to review for a third time the terms of a settlement agreement between the parties.

A. *The Decision Of The Court Of Appeals Does Not In Any Way Conflict With The Decision Of Any Other Circuit*

The petitioner does not dispute the standards of review utilized by the Court of Appeals in determining whether or not the District Court had abused its discretion in approving the settlement in question. Specifically, there is no dispute with the contention of the Court of Appeals that:

> "The most important of the factors to be considered in reviewing the settlement is the probability of success on the merits. Newman v. Stein, 464 F.2d 689, 692 (2d Cir.), cert. denied, 409 U.S. 1039 (1972). The likelihood of success, in turn, provides a gauge from which the benefits of the settlement must be measured. See Cotton v. Hinton, 559 F.2d 1326, 1330 (5th Cir. 1977)."

Petitioner's Appendix A p. 18.

A review of the probability of success requires a consideration of whether or not the shareholders would have succeeded in their argument that the directors of the corporation lacked the power to terminate the litigation in exercise of their business judgment. This the District Court did and the Court of Appeals so found. Petitioner's Appendix A p. 19. The petitioner contends that the Court of Appeals' analysis of the business judgment rule in the case *sub judice* conflicts with determinations in that area made both by the Sixth Circuit itself and the Second Circuit. What the petitioner fails to consider is that the business judgment rule is a matter of state law and that various interpretations of the rule reflect not differences between courts regarding interpretation of some uniform act, but rather reflect the varying difference in corporate law found in the fifty states. Thus, upon careful analysis the supposed conflict between the circuits is no conflict whatsoever.

The business judgment rule is derived from state corporate law and accordingly interpretation and application of that rule requires a federal court to look to the law of the state of incorporation of the company in question. *Burks* v. *Lasker*, 441

U.S. 471 (1979). As GenCorp. is incorporated in the State of Ohio the right of the director-respondents to terminate this litigation is dependent upon an interpretation of Ohio corporate law. In contrast, those cases the petitioner believes conflict with the case at bar involve examinations of the corporate laws of other states. See, *Hasan* v. *CleveTrust Realty Investors, et al.*, 548 F. Supp. 1146 (N.D. Ohio 1982), *vacated and remanded*, ___ F.2d ___ (6th Cir. 1984), [Petitioner's Appendix D], *reh. denied*, May 8, 1984, dealing with the law of Massachusetts; *Joy* v. *North*, 692 F.2d 880 (2d Cir. 1982), *cert. denied*, 103 Sup. Ct. 1498 sub. nom. *City Trust* v. *Joy* (1983), dealing with the law of Connecticut. The petitioner also cites to *Galef* v. *Alexander*, 615 F.2d 51 (2d Cir. 1980), a matter that dealt with an Ohio corporation but which is inapposite the case at bar as the Court of Appeals in that matter noted that Ohio law had not been argued before the District Court and that the case would have to be remanded for a full consideration of Ohio law. *Id.* at 62. Thus, even if there was in fact a conflict between the decision rendered in this case and that rendered in *Hasan* v. *CleveTrust Realty Investors, et al., supra*, and *Joy* v. *North, supra*, it is not the type of conflict between courts of appeals that may be a ground for the issuance of a Writ of *Certiorari*. As this Court has noted in the past:

> "As to questions controlled by state law, however, conflict among circuits is not of itself a reason for granting a writ of certiorari. The conflict may be merely corollary to a permissible difference of opinion in the state courts."

Ruhlin v. *New York Life Insurance Co.*, 304 U.S. 202 (1938) at 206.

Moreover, the perceived conflict that the petitioner sees with regard to the burden of demonstrating the good faith and independence of the directors who seek dismissal simply does not exist with regard to the various authorities cited by the petitioner. In contrast to cases such as *Hasan* and *Joy* the Court of Appeals below was not faced with a determination of a summary judgment motion. Rather, in evaluating the reasona-

bleness of the settlement it reviewed the District Court's analysis of the probabilities of success of the shareholders in prevailing in the matter. The Court of Appeals found that the District Court had adequately reviewed the independence of the outside directors and found no indication of any suspicious relationships between the outside directors and the inside management. Accordingly, it agreed with the District Court's determination that there was a slight possibility of the shareholders being successful in the litigation. This does not mean that had the matter come before the District Court on summary judgment the court would not have applied the proper standards and placed the varying burdens where they belong. Rather, the lower court recognized that neither the shareholder who initially brought the derivative actions nor the petitioner who sought to avoid termination of the actions had produced any evidence that was likely to persuade the court that the directors had failed to establish the requisite degree of independence. Thus, termination of the case unfavorably to the shareholders appeared inevitable regardless of whether the burden of establishing independence fell upon either the directors or the shareholders.

B. *The Court Should Not Exercise Its Power Of Supervision As The Lower Court's In This Matter Acted Properly In All Respects*

The petitioner requests that a Writ of *Certiorari* be granted in this matter because of alleged improprieties committed by both the District Court and the Court of Appeals. In doing so he seeks review under the criteria set forth in Rule 17.1(a) of the Rules of the Supreme Court, to wit:

> "(a) When a federal court of appeals...has so far departed from the accepted and usual course of judicial proceedings, or so far sanctioned such a departure by a lower court, as to call for an exercise of this Court's power of supervision."

The petitioner does not dispute the standards utilized by the

Court of Appeals in reviewing the decision of the District Court to approve the settlement. Clearly, the Court of Appeals would have been correct in setting aside the lower court's approval of the settlement only if it found that court to have committed a clear abuse of discretion. *Girsh* v. *Jepson*, 521 F.2d 153 (3rd Cir. 1975) at 156 n.7. In addition, there is no question that the District Court employed proper standards to evaluate the reasonableness of the settlement, *i.e.*, an evaluation of the benefits achieved by a settlement, the potential recovery that might have been achieved from a successful trial, the risks of the corporation receiving no benefit from any ultimate judgment, the complexity, length and expense of further litigation, the amount of opposition to the settlement. See, Order of the District Court Appendix SRA, p. 11; accord, *Protective Committee* v. *Anderson*, 390 U.S. 414 (1968) at 424. Thus, the petitioner disputes not so much the process utilized by the lower court to reach its decision but the decision itself.

It is difficult to understand under such circumstances how it can be said that the Court of Appeals has so far departed from the accepted and usual course of judicial proceedings as to justify this Court exercising its power of supervision. Moreover, the petitioners presents little to indicate that the lower courts erred in their evaluation of shareholders' probability of success on the merits. In the five years that elapsed between the filing of the initial derivative suits and the creation of the settlement agreement courts throughout the nation have recognized the propriety of allowing independent directors to terminate derivative suits against other members of the board of directors of the company under the business judgment rule. *Abramowitz* v. *Posner*, 672 F.2d 1025 (2d Cir. 1982); *Abbey* v. *Control Data Corporation*, 603 F 2d 724 (8th Cir. 1979), *cert. denied*, 444 U.S. 1017 (1980); *Lewis* v. *Anderson*, 615 F.2d 778 (9th Cir. 1979), *cert. denied*, 449 U.S. 869 (1980); *Genzel* v. *Cunningham*, 498 F. Supp. 682 (E.D. Mich. 1980).

The directors of GenCorp. that voted to terminate the shareholders' derivative litigation were not directly involved in

the improper conduct and did not personally benefit in any way from that conduct. Extensive discovery including depositions of the directors who voted to dismiss this action revealed no evidence to establish that the outside directors were not in fact independent of the inside management. These objective facts, which the petitioner has in no way been able to substantively challenge, led the shareholder respondents to the inevitable conclusion that the benefits conferred by the settlement were preferable to the inevitable dismissal of the derivative claims. This conclusion was buttressed by the later action of the District Court, which having conducted its own independent review and exercised its own business judgment as to the fairness of the settlement, concluded that the directors in question in all likelihood would have been found to have been independent and that the shareholders faced a very high risk of defeat on the merits if they sought to pursue their claims. Reviewing the actions of the District Court, the Court of Appeals also came to the conclusion that there was only a "slight possibility of a successful litigation, and that accordingly the district court had not abused its discretion in determining that the settlement was in fact reasonable, fair and adequate." Petitioner's Appendix A p. 18.

The settlement in question provides for the appointment of outside directors to RKO's Board of Directors and reflects the role played by the shareholders in bringing about various other remedial measures within the corporation. By restructuring the corporation to avoid future use of corporate assets to make secret and improper payments the settlement resolves one of the principal concerns of those who initiated the litigation. The alternative to this compromise was a the resumption of a complex, lengthy and expensive litigation that would almost inevitably have resulted in defeat of the derivative claims. Approval of the settlement in question hardly constitutes such a radical departure from the accepted and usual course of judicial proceedings as to warrant the intervention of this Court.

The petitioner also seeks review by this Court on the grounds that he was denied meaningful discovery with respect to the

settlement. He chooses to ignore the fact that he had available to him the transcripts of the depositions of the directors, an exhaustive report of a special review committee of the corporation and the opinions of two independent firms of outside counsel. As the Court of Appeals properly noted the District Court had assembled sufficient facts to intelligently approve the settlement and had allowed petitioner meaningful participation in the settlement hearing as well as the right to file additional written arguments following the hearing. Petitioner's Appendix A p. 16. This is all that is required with respect to a settlement hearing and petitioner gives no reason why he should have been entitled to rights greater than that afforded by established case law. See, *Detroit* v. *Grinnell Corporation*, 495 F.2d 448 (2d Cir. 1974) at 463. Further, the petitioner's request for discovery reveals what may well be his true motivation for seeking to prevent this case from coming to a close, *i.e.*, to obtain documents that may be of value to petitioner's counsel in any action to attack the broadcast license of RKO. See, Appendix SRA pp. 14-15.

Some three years ago counsel for shareholders in eight actions entered into an agreement with counsel for twelve defendants to bring what at that point was five year old litigation to an end. That settlement has in turn been approved after vigorous scrutiny by both the District Court and the Court of Appeals. A single shareholder, whose counsel's motivations are suspect, should not be allowed to prevent consummation of the settlement that is clearly in the best interests of all parties.

CONCLUSION

For all the foregoing reasons the shareholder respondents respectfully request that the Petition of Writ of *Certiorari* be denied.

DATED: August 30, 1984

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APPENDIX

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In Re:	:	MDL No. 265
THE GENERAL TIRE AND RUBBER SECURITIES LITIGATION	:	ORDER

Battisti, C.J.

The controversy before this Court today consists of five shareholder derivative suits filed for the benefit of the General Tire and Rubber Company ("General Tire", "the Company").[1] In 1977 and in 1980, special committees appointed by the Company to oversee the litigation recommended that the continued prosecution of the suits would not be in the best interests of General Tire. Invoking the business judgment rule, the board of directors, minus certain individuals with demonstrated personal interest in the litigation, adopted the recommendations and dropped the suits. Thereafter, in 1981, the Plaintiffs in these actions arrived at a settlement proposal with the Company. Other shareholders have appeared before the Court to attack both the legality of the directors' dismissals of the suits and the fairness to the Company of the settlement proposal itself. That proposal, which has been submitted to the Court for approval, is the subject of this order. The Court observes first, without deciding, that the directors very likely had power to dismiss the derivative suits under the business judgment

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[1] *Kramer v. General Tire & Rubber Co.*, No. C77-395 (N.D. Ohio, filed Apr. 27, 1977); *Lewis v. O'Neil*, No. C77-374 (N.D. Ohio, filed Apr. 14, 1977); *Cohn v. O'Neil*, No. C77-396 (N.D. Ohio, filed April 27, 1977); *Milberg v. General Tire & Rubber Co.*, No. C77-397 (N.D. Ohio, filed Apr. 25, 1977); *Monheit v. O'Neil*, No. C81-1441 (N.D. Ohio, filed Jul. 17, 1981).

rule. Secondly, as measured by the considerations expressed in federal law and policy, the Court finds the settlement proposal to be fair, reasonable, adequate, and in the best interests of General Tire. Accordingly, the complaints in these actions are dismissed on the merits and with prejudice.

I.

The present litigation arises out of corporate misfeasance of many years' standing. Throughout the 1960's and into the early years of the 1970's, General Tire engaged in an extraordinary scale of improper and apparently illegal activities, both within the United States and in other countries. The Company's wrongdoing attracted the attention of the Securities and Exchange Commission, and civil proceedings were eventually initiated. On May 10, 1976, the action was settled by the parties with the approval of the United States District Court in Washington, D.C. The Company was permanently enjoined from similar violations in the future, and General Tire agreed to establish a Special Review Committee ("SRC", "the Committee") to examine the suspect activities and submit a detailed report.

The resulting report was submitted to the chairman of the board of General Tire on July 1, 1977. Pursuant to its recommendations, a number of officers and employees paid the Company a total of $337,260 as reimbursement for corporate funds which they had used for unlawful domestic political contributions. The Company also established procedures and guidelines to avoid any repetition of what had occurred.

In the aftermath of the SEC permanent injunction and consent decree, shareholders of General Tire filed four separate derivative suits – the four 1977 – dated cases currently before this Court. The suits alleged injury to General Tire as a result of the unlawful or improper activities in which the Company had been engaged. The Judicial Panel on Multi-District Litigation consolidated the suits in the Northern District of Ohio under the present caption on April 18, 1977.

On July 1, 1977 – the same day it submitted its report – the Special Review Committee notified the full board as to which members of the board it had concluded to be sufficiently independent of the actions discussed in the report to be capable of reviewing it and taking any implementing action necessary. On July 14, the six directors who had been approved by the Committee voted on behalf of the board to adopt and implement the Committee's recommendations. On October 24, the Bricker and Eckler law firm of Columbus, Ohio, advised the Committee that the latter was vested as a matter of business judgment with the authority to determine whether the Company should, or should not, pursue the derivative claims. Three days later, the Committee determined that further prosecution of the suits was not in the best interests of the Company. The independent directors thereupon instructed counsel to move for dismissal of the litigation.

The Company and various individual Defendants moved this Court for summary judgment, claiming that the independent directors had exercised their business judgment in a lawful manner. Further discovery was stayed pending decision on these motions. Plaintiffs' attorneys contested both the availability of the business judgment rule and the independence of the directors in question. In March, 1981, the Court ordered further discovery on independence, limiting such discovery to the use of depositions, documents, and interrogatories. Plaintiffs' attorneys issued numerous interrogatories and filed four depositions with the Court.

The Special Review Committee's report also led to the filing of a somewhat different lawsuit. RKO General, Inc., ("RKO") is a wholly-owned, unconsolidated subsidiary of General Tire. On January 24, 1980, the Federal Communications Commission denied RKO's application for renewal of the licenses to three of its television stations. The FCC's denial was explicitly based upon the record of improprieties and/or illegalities contained within the Committee's report, see Exhibit G, Affidavit of John J. Dalton, *Barr v. O'Neil*, No.02040/80, N.Y. Supr. Ct., N.Y. Cty.

Thereafter, on February 14, 1980, a double derivative suit was filed in the Southern District of New York on behalf of General Tire and RKO. For the most part, the complaint was intended to redress the damages incurred by these firms as a result of the FCC's decision. Plaintiffs served various discovery requests upon Defendants, including requests for production of documents, interrogatories, and a detailed request for admissions of fact. On February 28, 1980, the board of General Tire appointed a Special Litigation Committee to investigate the suits. The Committee consisted of two new directors appointed to the board in 1978. On March 27, 1980, again at the advice of the Bricker and Eckler law firm, this Committee recommended that the Company invoke the business judgment rule for the purpose of dismissing the new suit. On the same day, the seven directors now conceived to be independent adopted the recommendation. Defendants filed motions to dismiss and also a motion for summary judgment pursuant to the business judgment rule. To these motions, Plaintiffs took vigorous exception. The case has subsequently been transferred to this district for purposes of the present settlement proceedings.

The additional discovery undertaken by the Plaintiffs of the four earlier suits evidently convinced them that further prosecution would be fruitless. On June 25, 1981 the parties presented for approval to this Court a Stipulation of Settlement. The Court entered an order directing that a hearing be held pursuant to Rule 23.1 of the Federal Rules of Civil Procedure in order to determine whether the proposed settlement was fair, reasonable, and adequate, and whether judgment should be entered dismissing these actions on the merits and with prejudice. The hearing was held on August 18, 1981.

Notice of the hearing was properly served upon the shareholders of General Tire. Shareholders John J. and Curtiss R. Pearl, Anne W. Rose, George Schreiber, J.A. Lockhart, and Howard L. Shuken filed objections to the proposed settlement, and John J. and Curtiss R. Pearl and George Schreiber appeared by counsel at the hearing to oppose the approval of the settlement. The Court received inquiries and suggestions from two

other people who did not allege shareholder status.

Following the hearing, the Court directed the parties and objectors to submit proposed orders by means of which this litigation might be resolved. The parties provided an order supporting the settlement arrangements. The Pearls submitted an order, the gist of which is that the settlement as it presently stands is premature. George Schreiber produced another order rejecting the settlement as inadequate. The bulk of his order, however, as well as the additional briefing he has submitted, consist of further arguments against the applicability of the business judgment rule in these proceedings, and against the independence of these directors should the rule be found applicable.

II.

The Court conceives essentially one issue in this litigation – namely, whether the proposed settlement is fair, reasonable, and adequate. Before addressing this question, however, the Court will devote some attention to the logically prior issue of whether the directors' dismissals of the shareholder suits were lawful. It must be emphasized at this point, however, that the Court's observations with respect to the legitimacy of the dismissals do not constitute determinations on the merits. Plaintiffs have already decided to settle with the Company, and the adequacy of Plaintiffs' representation of the shareholders in reaching this decision has been upheld in the prior order of this Court. Hence the business judgment rule, and the actual independence of the outside directors in this litigation, are not properly before the Court at this stage. Nonetheless, a fair consideration of the dismissal of the suits is appropriate, in view of the extended argumentation which Plaintiffs, Defendants, and Objectors have lavished upon this issue. The Court finds that Defendants had a strong likelihood for success on the merits of their motion for summary judgment.

Controversies involving the power of corporate directors –

even, as here, where violations of federal law are alleged[2] – are ordinarily determined under applicable state law, *Burks v. Lasker*, 441 U.S. 471, 479 (1979). No claim has been made at this stage of the proceedings that any state law other than that of Ohio is applicable here.[3] The Ohio formulation of the business judgment doctrine is crystal clear. The board of directors of a corporation is vested with general authority to determine when actions shall be prosecuted or defended on behalf of the corporation, *Wadsworth v. Davis*, 13 Ohio St. 123 (1862); 11 Ohio Jur. 3d § 393. A given board may decide in good faith in the exercise of its discretion to refuse to bring suit against the corporation, and courts may not challenge this refusal unless it is "wrongful, fraudulent, and arbitrary," *Cooper v. Central Alloy Steel Corp.*, 43 Ohio App. 455, 183 N.E. 439 (1931); *Roderick v. Canton Hog Ranch Co.* 46 Ohio App. 475, 480-481, 189 N.E. 669 (1933). More precisely, when the directors are in an unbiased position and act in good faith, the wisdom of their decision will not be reviewed by the courts, *Rice v. Wheeling Dollar Savings & Trust Co.*, 71 Ohio L. Abs. 205, 214, 130 N.E. 2d 442 (1954); see also W. Fletcher, Cyclopedia of the Law of Private Corporations §5929.2 (rev. perm. ed. 1975). Contrary to the suggestion of Objector Schreiber, see Objection to Proposed Settlement at 6, the recent case of *Galef v. Alexander*, 615 F.2d 51 (2d Cir. 1980), casts no doubt upon the strength of the business judgment rule in Ohio. The Second Circuit expressly reiterated the

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[2]The 1977 suits allege, *inter alia*, violations of Sections 10(b), 12(b)(1), 13(a), and 14(a) of the Securities Exchange Act of 1934, as amended, 14 U.S.C. §78a *et seq.*, and regulations thereunder.

[3]The *Monheit* plaintiffs had argued for the application of Delaware law, *see* Plaintiffs' Memorandum in Opposition to Defendants' Motions to Dismiss at 19. The Pearls do not renew that argument. Mr. Schreiber recognizes the applicability of Ohio law, *see* Objection to Proposed Settlement at 6-7. Defendants, of course, have argued the business judgment doctrine in terms of Ohio law throughout this litigation.

general formulation that a good faith determination of a disinterested majority of the board to dismiss the derivative action ought not to be reviewed by the courts, *id.* at 57. More particularly, the *Galef* court concluded from its survey of Ohio law that non-defendant directors are apparently capable of dismissing such motions under the business judgment rule, *id.* at 64, n. 20. The directors who voted to dismiss the suits pending here are named Defendants in several instances.[4] However, the court cited with approval other federal cases for the proposition that merely nominal defendants, against whom no relief is asserted, or who did not benefit from the challenged transactions, should properly be considered disinterested, *id.* at 60, n. 17. As succeeding paragraphs will indicate, this Court finds little in the facts before it to suggest that reasonable claims for relief could be asserted against the outside directors in these cases. Nor is there any allegation that they have benefitted from the improprieties and/or illegalities catalogued in the Special Review Committee's report. Therefore, this Court would interpret *Galef* to support dismissal of these suits by the named Defendants on the facts given.

Objector Schreiber also argues that federal policy precludes summary dismissal via the business judgment rule of claims arising under section 14(a) of the 1934 Securities Exchange Act, Additional Brief of September 11, 1981 at 2, citing *Galef v. Alexander;* see also *Lewis v. Anderson,* 615 F.2d 778 (9th Cir. 1979). It is true that state law must give way to federal law when application of the former would be inconsistent with federal policy, *Burks v. Lasker,* 441 U.S. 471 at 479. It is also clear that the safeguarding of shareholders from false or misleading proxy information — the basis of section 14(a) — is a vital component of the federal securities laws. Nonetheless, this Court would not invalidate the dismissal and compromise

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[4]Mssrs. L.D. Henry, D.B. Mansfield, J.T. Morely, and W.B. Walsh are named Defendants in *Milberg, Cohn,* and *Monheit.* D.S. Henkel is named in *Milberg* and *Cohn.*

of these suits on the purely formal basis that section 14(a) claims are present.

The facts of this litigation appear insufficient to support any reasonable allegation of responsibility on the part of the outside directors for the underlying misfeasances committed by the Company. Plaintiffs contend that the Company's proxy materials were false and/or misleading precisely because they accompanied and disguised these misfeasances, see e.g. *Cohn* Complaint at 22; *Milberg* Complaint at 6. This Court can find no better basis for attributing to the directors the deceptive proxy information than to the underlying conduct itself.

The cases cited by Mr. Schreiber are not binding in this circuit. Insofar as they establish a rigid restriction upon the directors' discretion based upon the formal presence of section 14(a) allegations, this Court would decline to follow them. The Court conceives in the facts before it no conflict between the business judgment doctrine and the federal policy of safeguarding the integrity of proxy materials.

Directors of a corporation are presumed to act in good faith, *Corbus v. Alaska Treadwell Gold Mining Co.*, 187 U.S. 455 (1903). The good faith of these directors has not been seriously challenged.[5] Objectors are therefore thrown back upon the argument that these individuals were in some way disabled, by bias or personal considerations, from rendering disinterested judgment when they decided to dismiss the suits, *Rice v. Wheeling Dollar Savings & Trust Co.*, 71 Ohio L. Abs. 205.

Objector Schreiber attacks the independence of the outside directors who constituted the Special Review Committee and who voted to dismiss the *Kramer*, *Milberg*, *Cohn*, and *Lewis* suits in 1977, Objection to Proposed Settlement at 8-12; Re-

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[5]Objector Schreiber does indeed question the good faith of J.J. Dalton, Secretary and General Counsel of General Tire, Objection to Proposed Settlement at 12-15. The Court finds no need to indulge this inquiry with regard to Mr. Dalton. The Court sees no basis whatsoever for attributing Mr. Dalton's good faith, or lack of it, to the outside directors.

sponse of George Brooks Schreiber to the Court's Requests at 2-4. He cites as justification the depositions of T.F. O'Neil, M.G. O'Neil, D.B. Mansfield, and C.C. Hoskins (a partner in the Bricker and Eckler law firm). The Court has examined these depositions for indications of suspicious relationships between these outside directors and the inside management of General Tire, and has found none.

Mssrs. Henry and Morely appear to have known T.F. O'Neil, former chairman of the board of General Tire, for many years, and to have maintained some cursory social contact with him, Deposition of T.F. O'Neil at 17 and 19. Mr. Henkel provided legal assistance to the Company as outside counsel for securities - related matters for many years, Deposition of T.F. O'Neil at 8-10. These relationships in themselves would seem insufficient to establish bias in the outside directors, or control of them by inside management. On the contrary, there is little, if any, evidence to temper their appearance of being upright, responsible leaders in the business and civic communities. Plaintiffs themselves determined, after having taken these four depositions, that these individuals were in fact independent, Plaintiffs' Memorandum in Support of Proposed Settlement at 4-5. The Court sees no reason to question their conclusion.

It also deserves emphasis that four of the five outside directors who voted to dismiss in 1977 were appointed to the board in 1975 – after the improper or illegal conduct alleged in the complaints filed in these actions, and in the complaint filed by the SEC.[n] They could not have been involved in that conduct.

Finally, Mr. Schreiber vigorously challenges the independence of Mr. Lester Garvin, who was appointed to the board in 1978, and who participated in the dismissal of the *Monheit* suit. He argues that Mr. Garvin was deeply involved in the improper practices engaged by the Company in Chile, which

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[n]L.D. Henry was appointed in 1973.

were catalogued in the Special Review Committee's report, Report at 121-161; Objection to Proposed Settlement at 12-14. In response, the Company asserts that Mr. Garvin was hired as an "independent consultant" for Chilean matters; that his identity as such was properly described in General Tire's proxy materials; and that his role in Chile in 1974-1975 consisted of investigating improprieties which had already taken place, Memorandum of the General Tire & Rubber Company in Support of Settlement at 8-9. The Company also points to the interview of Mr. Garvin by the Bricker and Eckler firm, which led the latter to conclude unequivocally that Mr. Garvin was not associated in any way with the events described in the Special Review Committee's report, *id.* at 9; Deposition of C.C. Hoskins at 31 and 39; Exhibit J, Affidavit of John J. Dalton, *Barr v. O'Neil,* No.02040/80, N.Y. Supr. Ct., N.Y. Cty.

The evidence as it now stands would not be sufficient for this Court to conclude that Mr. Garvin was too biased or personally interested in the *Monheit* suit to recommend its dismissal. As discussed in previous pages, *Monheit* is primarily a claim for damages against General Tire, based upon the FCC's refusal to renew three licenses of RKO General. The FCC's refusal was founded explicitly upon the record compiled in the SRC report. That report was authored by outside directors whom the Court has already suggested to have been independent. It tracks General Tire's Chilean adventures in considerable detail for some forty pages, Report at 121-161. Nowhere does the name Garvin appear. Mr. Garvin was not a director or even an internal employee of General Tire when he was employed in Chile in 1974-1975. He was not named as a Defendant in *Monheit*. On this record, the likelihood that Mr. Garvin was unable to render a disinterested appraisal of the value of dismissing that suit simply does not appear reasonable.

In summary, it is not necessary at this point for the Court to determine whether the directors in question were independent. Nor does the Court do so here. The foregoing has been included herein to assure the Objectors who came forward

with these concerns that the Court has given fair consideration to their arguments, and finds nothing to indicate that the settlement ought not to be approved. The Court now passes to the propriety of the settlement proposal currently submitted for approval.

III.

Federal Rule of Civil Procedure 23.1 leaves the approval of compromise settlements to the sound discretion of the court, *United Founders Life Ins. Co. v. Consumers National Life Ins. Co.*, 447 F.2d 647 (7th Cir. 1971); 3B Moore's Federal Practice § 23.1.24 [2] (2d ed. 1981) at 132-133. The Rule places the Court in the position of a third party to the compromise, and a guardian of the corporation's interest, *Masterson v. Pergament*, 203 F.2d 315 (6th Cir. 1953), *cert. denied*, 346 U.S. 832 (1953); *Norman v. McKee*, 290 F. Supp. 29 (N.D. Cal. 1968), *affirmed*, 431 F.2d 769 (9th Cir. 1970), *cert. denied sub nom. Security Pacific National Bank v. Myers*, 401 U.S. 912 (1971). Proponents of the settlement have the burden of persuading the court that their compromise is fair, reasonable, and adequate, *Cotton v. Hinton*, 559 F.2d 1326, 1330 (5th Cir. 1977).

In evaluating the reasonableness of such a proposal, courts are guided by several considerations. Perhaps most important is a comparison between the benefits achieved by the settlement as offered, the potential recovery which might follow a successful trial, and the risks to the corporation of recovering nothing, *Newman v. Stein*, 464 F.2d 689 (2d Cir. 1972), *cert. denied*, 409 U.S. 1039 (1972); *West Virginia v. Chas. Pfizer & Co.*, 314 F. Supp. 710 (S.D. N.Y. 1970), *affirmed*, 440 F.2d 1079 (2d Cir. 1971), *cert. denied sub nom. Cotler Drugs v. Chas. Pfizer & Co.*, 404 U.S. 871 (1971). Other significant factors include the complexity, length, and expense of further litigation, and the amount of opposition to the settlement, *Grunin v. International House of Pancakes*, 513 F.2d 114 (8th Cir. 1975), *cert. denied*, 423 U.S. 864 (1975); *Manual for Complex*

Litigation at 56. The prevailing flavor of the cases reveals a preference for the voluntary resolution of litigation through settlement. Especially is this true with respect to shareholder litigation, which is notoriously difficult and uncertain, *Lewis v. Newman*, 59 F.R.D. 525 (S.D. N.Y. 1973).

The settlement proposed to this Court acknowledges the role which the derivative suits have played both in causing the Company to make reparations pursuant to the consent decree in the SEC suit, and in establishing the ordered, legal guidelines and procedures which are now followed by the Company. It also mandates that for a period of at least three years two new outside directors will sit on the board of RKO General. In addition, the settlement calls for a ceiling of $500,000 in attorneys' fees for Plaintiffs' counsel, plus expenses. Plaintiffs' counsel has subsequently petitioned the court for the full $500,000 plus disbursements in the sum of $20,814.50.

It is the opinion of this Court, based upon the considerations just enunciated, that the proposed settlement is a reasonable one. This is not to suggest that the formula arrived at by the parties is ideal. The shortcomings of this arrangement are obvious and counsel for Mr. Schreiber and the Pearls have levelled appropriate assaults upon them, Transcript of Proceedings at 31-34 and at 76. No monetary recovery to the corporation is contemplated in this settlement. Although Plaintiffs are surely correct in maintaining that court approval is not dependent upon an exchange of funds, see Plaintiffs' Memorandum of Support at 27-34 and cases cited therein, this principle can hardly add luster to the deal. The corporate therapeutics upon which Plaintiffs lay such emphasis, *id.* at 12-15, were largely the result of the Company's own Special Review Committee, Report at 18-24.

Nevertheless, the proposed settlement has several advantages to recommend it. In the first place, although this Court has been careful to avoid a determination of the outside directors' independence, it is clear that Plaintiffs would have faced considerable difficulties had they brought this litigation to trial. In light of the record provided, the premonition of an adverse

summary judgment in the thinking of Plaintiffs' counsel cannot be faulted. If little new is afforded by the settlement, the high risk of defeat on the merits is also avoided.

The settlement does provide some benefit to the Company not prefigured in the SRC's report. The addition of outside directors to the board of RKO General may well ensure more responsible behavior in this subsidiary. In any event, the Court will not second-guess the quality of concessions extracted by Plaintiffs from Defendants, *Glicken v. Bradford*, 35 F.R.D. 144 (S.D. N.Y. 1964). It may be that this particular concession represented the farthest limit of the possible for these Plaintiffs, in view of the bargaining limitations inherent in their legal position.

The Court is also impressed with the number of objectors and the quality of their objections. At this point in the proceedings, only Mr. Schreiber and the Pearls have actively submitted proposed orders for the Court. The remaining objectors (as well, of course, as the original Plaintiffs) have melted out of the controversy. Although not definitive, this small number of objectors implies the acceptability of the settlement to the vast majority of shareholders, *Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173, 1178 (9th Cir. 1977).

The gravamen of the Pearls' objection is that this settlement is premature. They argue that the Court's approval ought to be delayed pending the outcome of numerous other proceedings before the FCC and the Internal Revenue Service involving General Tire and RKO General. Only thus can a fair comparison be drawn between the terms of this settlement and the actual losses sustained by General Tire and its subsidiary, see Proposed Order; Transcript of Proceedings at 57 *et seq.*

The Court finds the utility of this argument absurd. Thirteen more broadcast licenses are potentially subject to revocation by the FCC; if all thirteen are challenged and argued through full administrative and court proceedings, the results will not be known for many years. As a representative of the interests of the Company, this Court cannot permit such a sword of Damocles to be suspended above the directors and management

of General Tire. To rule otherwise would establish a longterm, destructive impediment to the exercise of their business judgment in the day-to-day operations of the firm.

As for Mr. Schreiber, the Court expressed repeated concern at the hearing as to the ultimate purpose of his objection, Transcript of Proceedings at 49-51 and 111. Subsequent briefs and motions have not alleviated that concern. Mr. Schreiber's greatest emphasis has been placed upon the need for access to the working papers upon which the SRC based its report in 1977. These papers are under the control and custody of the Cleveland law firm of Baker and Hostetler. In the original SEC investigation, Judge George L. Hart, Jr., of the United States District Court for the District of Columbia ordered the papers sealed. Judge Hart was concerned with the need to protect American and foreign nationals whose lives might be jeopardized if the papers were released. He has since maintained the papers under seal.

Party counsel claim, however, that Mr. Schreiber's attorney, Steven R. Rivkin, Esq., has a mixed motive for seeking access to these materials. In its Memorandum in Support of Settlement, the Company claims that "until three weeks ago [Mr. Rivkin] was counsel of record before the FCC on behalf of a company [New South Media Corporation] seeking vigorously to have all of RKO's broadcast licenses revoked," at 12. Mr. Rivkin argued that the FCC's decision to revoke one license is grounds for the revocation of the licenses of all thirteen RKO stations, and he "filed a request to the FCC to investigate RKO's tax dispute with the IRS as another possible ground for RKO's disqualification as a broadcast licensee," *id.* Additionally, General Tire notes that prior to representing New South Media, Mr. Rivkin was counsel for HUB Broadcasting when it challenged RKO's Boston television license. General Tire claims that rather than believing that access to the working papers is necessary to represent Mr. Schreiber and other shareholders here, "(a) more likely use of those files would be further muckracking of General Tire's past, such as that done in the past by Mr. Rivkin and his colleagues in the FCC

proceeding," *id.* at 13, footnote. Similar allegations as to Mr. Rivkin's prior representation and motives were made at the hearing. Mr. Rivkin did not deny his prior involvement with HUB or New South Media.

This Court will not attempt to decide whether Mr. Rivkin is, in fact, currently engaged in conflict-burdened representation. However, a court must determine whether a shareholder in a derivative action fairly and adequately represents the interests of the company, see, e.g., *David v. Comed, Inc.*, 619 F.2d 588 (6th Cir. 1980) (where the court found that plaintiffs were acting as a front for others whose interests were inimical to the interests of the shareholders). For that reason, it is necessary for the Court to take notice of the motives of the shareholders' attorney here. It appears that there is good cause to believe that Mr. Schreiber is not able to fairly and adequately represent the interests of the Company. The Federal Rule is clear that in such circumstances the derivative suits ought not to be maintained, Fed. R. Civ. P. 23.1.

The foregoing discussion leads this Court to believe that the objections of the Pearls and of Mr. Schreiber are without merit. Accordingly, the Stipulation of Settlement presented on June 25, 1981, is hereby approved.

The complaints in these actions are dismissed on the merits and with prejudice and without costs. The order entered today represents a full and final discharge against all persons whatsoever of any and all claims which were, or could have been, alleged in the complaints, by reason of, in connection with, or which arise out of the matters or transactions set forth or referred to.

In accordance with the Stipulation of Settlement, and for a period of three years from the date of consummation of the settlement, Defendant RKO General, Inc., will maintain as members of its board of directors at least two persons who are not officers or employees of that corporation.

Having considered applications by Plaintiffs for the allowance of counsel fees and disbursements, the Court authorizes counsel's fees in the amount of $500,000 and disbursements

in the amount of $20,814.30. Said amounts will be paid by Defendant General Tire at the time and in the manner specified in the Stipulation of Settlement.

The Court retains jurisdiction to enter such further orders as may be necessary to carry out the Stipulation of Settlement.

IT IS SO ORDERED.

Frank J. Battisti
Chief Judge